

KEEGAN, WERLIN & PABIAN, LLP

ATTORNEYS AT LAW
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BOSTON, MASSACHUSETTS 02110-3525

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(617) 951-1354
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August 1, 2003

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station
Boston, MA 02110

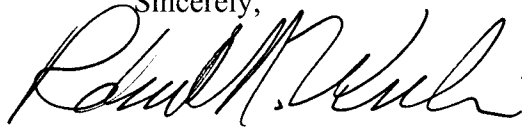
Re: D.T.E. 03-47, Boston Edison Company, Cambridge Electric Light Company,
Commonwealth Electric Company, NSTAR Gas Company, Pension/PBOP
Adjustment Mechanism Tariff Filing

Dear Secretary Cottrell:

Enclosed for filing in the above-referenced matter are the responses to the
Information Requests set forth on the accompanying list.

Thank you for your attention to this matter.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert N. Werlin". The signature is fluid and cursive, with the first name "Robert" being the most prominent.

Robert N. Werlin

Enclosures

cc: Service List

Responses to Information Requests

Information Request AG-2-1

Information Request AG-2-2

Information Request AG-2-3

Information Request AG-2-4

Information Request AG-2-5

Information Request AG-2-6

Information Request AG-2-7

Information Request AG-2-8

Information Request AG-2-1

Please provide a copy of Mr. Spear's curriculum vitae.

Response

Mr. Spear's curriculum vitae has been included as Attachment AG-2-1 to this document.

Attachment AG-2-1

**Robert J. Spear, CPA
PricewaterhouseCoopers LLP
One International Place
Boston, MA 02110**

Experience

**December 1991 to Present
Boston, MA**

Audit Partner

- ◆ Industry experience includes regulated utility , construction and engineering, retail and wholesale, healthcare and higher education. Significant experience in dealing with large decentralized organizations.
- ◆ Experience in merger and acquisition accounting, contract accounting, SEC reporting and preparedness and due diligence reviews.
- ◆ Responsible for implementing the use of proprietary technology in a variety of industry groups.
- ◆ Involvement in several high profile client investigations in response to public allegations of potential conflicts of interest and violations of laws and regulations.
- ◆ Responsible for coordinating technical training programs.
- ◆ Frequent instructor in firm-related training courses.
- ◆ Selected as firm representative on the Not-for-Profit Committee of the American Institute of Certified Public Accountants.

**September 1988 to December 1991
New York National Office**

Audit Partner (Admitted October 1, 1988)

- ◆ Selected to participate in a two-year rotational program in the National Office. Assignment was extended to 3 1/2 years.
- ◆ Served as project partner on a three-year landmark study with the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Co-authored research study, Internal Control-Integrated Framework, 1992 by the Committee of Sponsoring Organizations of the Treadway Commission.
- ◆ Participated in the development of technical accounting standards being considered by the Financial Accounting Standards Board (FASB). Testified at the FASB on the project, Impairment of Long-Lived Assets.
- ◆ Developed a National Technical Update session for all C&L offices and selected foreign offices.
- ◆ Numerous public speaking engagements on internal control concepts (COSO) and technical accounting and auditing developments. Presentations made to groups ranging from 50-250.

Attachment AG-2-1 - Continued

Robert J. Spear, CPA

Page 2

**September 1978 to September 1988
Portland, ME**

Staff Accountant to Manager

- ◆ Promoted to manager in 5 1/2 years.
- ◆ Experience with organizations in the retail and wholesale distribution, manufacturing and higher education industries.

Education and Affiliations

- ◆ Bachelor of Science in Business Administration, May 1978, Whittemore School of Business and Economics, University of New Hampshire
- ◆ Dartmouth College, Tuck Executive Program
- ◆ American Institute of Certified Public Accountants
- ◆ Massachusetts, New York, New Jersey, Rhode Island, Connecticut, New Hampshire and Maine State Societies of CPAs

Information Request AG-2-2

Please provide a list of the firms and the dates of those engagements when Mr. Spear has been the engagement partner on an audit for the last ten years.

Response

A listing of the firms and the dates of those engagements when Mr. Spear has been the engagement partner on an audit for the last ten years has been included in Attachment AG-2-2 to this document.

Attachment AG-2-2

Robert J. Spear – Clients

Client	Engagement Partner	
	From	To
NSTAR	2000	Present
Camp Dresser & McKee	1999	Present
Trevi Icos Corporation	1998	Present
Shaw's Supermarkets, Inc.	1996	2000
Stone & Webster	1992	Present
Puma North America	1994	1998
Harvard University and affiliated entities	1992	1998
Designs, Inc.	1996	1998
Datex Engstrom, Inc.	1994	1998
Boston University	2003	Present
Dartmouth College	1992	1999
Museum of Fine Arts	2000	Present
Museum of Modern Art	1999	Present
Anna Jaques Hospital	1997	2000
Back Bay Restaurant Group	1995	1999
Boston Medical Center	1996	1999
Carleton-Willard Homes	1995	1999
Center for Blood Research	1995	1999
Childreach	1998	Present
Educational Testing Service	1999	2000
Elderhostel, Inc.	1992	1999
Emerson Hospital	1998	Present
Fairleigh Dickinson University	1999	2001
Faulkner Hospital	1992	1998
Guggenheim Museum	1999	2001
Jordan Hospital	1992	1999
Lawrence General Hospital	1996	Present
Maine Medical Center Affiliates	2001	Present
Mass Eye & Ear Infirmary	1996	1999
Metropolitan Museum of Art	1999	Present
New School University	1999	2002
Pathfinder International	1992	2002
Princeton Theological Seminary	1999	2001
Quincy Medical Center	1999	Present
St. Paul's School	1995	1999
Wheaton College	1992	2000

Information Request AG-2-3

Please provide copies of all testimony that Mr. Spear has provided before a regulatory body on the same or similar topic(s) as submitted by Mr. Spear in this proceeding.

Response

Mr. Spear has not provided any testimony before a regulatory body on the same or similar topic as submitted by Mr. Spear in this proceeding.

Information Request AG-2-4

Please itemize and quantify the cost of all services provided by PricewaterhouseCoopers and each of its affiliates and subsidiaries to NSTAR, its predecessors and each of their affiliates, and subsidiaries in each of the last five years.

Response

The cost of all services provided by PricewaterhouseCoopers to the Company in each of the last five years is as follows:

Year	Fee Category (a)			
	Audit	Information Technology	Other	Total
2002	\$780,000	\$0	\$264,000	\$1,044,000
2001	\$593,000	\$0	\$216,100	\$809,100
2000	\$641,600	\$0	\$181,200	\$822,800
1999	\$651,700	\$0	\$351,200	\$1,002,900
1998	\$487,100	0	\$283,300	\$770,400

(a) Fee categories presented above are in accordance with the proxy disclosure rules as defined by the Securities & Exchange Commission.

(b) The category "Other" includes fees related to the annual financial statement audits of the Company's benefit plans, agreed-upon procedures performed in connection with various debt offerings, and various accounting and tax issues reviewed with the Company.

Information Request AG-2-5

Please provide a complete and detailed description of Mr. Spear's fee arrangement for his testimony in this case. Please also provide a copy of any engagement letters.

Response

The fee arrangement for Mr. Spear's testimony in this case is based on actual hours incurred by PricewaterhouseCoopers (PwC) in providing the direct testimony to the Department, as well as responding to information requests associated with the filing. All hours incurred will be billed to the Company at approximately 60% of PwC's standard billing rates. We have informed the Company that we estimate the cost of all services associated with the testimony and related information requests to be approximately \$20,000 - \$50,000. See the Attachment to the response to Information Request AG-2-8 for the agreement between the Company and PwC for Mr. Spear's testimony.

Information Request AG-2-6

Please provide copies of all workpapers, analyses, memorandum, and e-mails generated by PricewaterhouseCoopers and any of their employees regarding the original deferral requested in D.T.E. 02-78 and the proposal for recovery in this case.

Response

A copy of the workpapers generated by PricewaterhouseCoopers regarding the original deferral requested in D.T.E. 02-78 and the proposal for recovery in this case has been included in Attachment AG-2-6 to this document.



Robert J. Spear
01/01/2003 12:02 PM
617-478-5294
Boston
US

To: John H McCarthy/US/ABAS/PwC@Americas-US, Simon R.
Gerlin/US/ABAS/PwC@Americas-US
cc: Sean P Riley/US/ABAS/PwC@Americas-US
Subject: Re: DTE approval of accounting order

Jack and Simon:

We were able to conclude favorably on the NSTAR pension issue. Good news for the Company, they will be pleased. I do need to work with Bob Weafer on the Company's representation letter, and with external Rate Council to finalize their opinion letter but I expect that will move along smoothly given the draft opinion we already have coupled with the discussion that have been ongoing for some time.

Sean: we need to prepare a final memo documenting our discussions/consultations. Let's do this in the next week or so.

Hope you are having a great new year.

Bob

----- Forwarded by Robert J. Spear/US/ABAS/PwC on 01/01/2003 11:52 AM -----



Randall J. Vitray
12/31/2002 01:25 PM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc: Sean P Riley/US/ABAS/PwC@Americas-US
Subject: Re: DTE approval of accounting order

Sounds good to me.

This also sounds like a good precedent for the industry. Can you forward this to Casey Herman for that purpose?

Robert J. Spear



Robert J. Spear
12/31/2002 11:48 AM
617-478-5294
Boston
US

To: Randall J. Vitray/US/ABAS/PwC@Americas-US
cc: Sean P Riley/US/ABAS/PwC@Americas-US
Subject: Re: DTE approval of accounting order

I spoke with management last night as to the analysis of a favorable rate recovery. Both management and Rate Council believe that the AG will be the only intervener in this case and, based on past experiences and legal precedent, they believe the Company will prevail. Based on that analysis, Rate Council has issued a strong legal opinion (i.e. recovery is probable) as to recovery. That analysis contemplated the point you are making regarding the DTE's past practice of allowing costs to be recovered as contributions to the plan are being made. They (management and Rate Council) are comfortable that the DTE will allow recovery of the increased costs (as a side note, they point to the fact the all 5 commissioners signed the accounting order, which is somewhat unusual and points to a strong consensus; many times the commissioner's votes are split).

Management is prepared to provide the representations we need regarding these points (up to the CEO level). Rate Council believes it has provided a strongly worded opinion, but they are open to discussions of any other wording we may need. Also, a plan has been put in place for the Company to file for a rate case by mid-March/April (the timing of our audit of the FERC Form 1s has been accelerated to facilitate this filing date).

I believe we have the support we need. Let me know what you think.

Thanks,
Bob

Randall J. Vitray



Randall J. Vitray
12/30/2002 05:02 PM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc:
Subject: Re: DTE approval of accounting order

I looked at the material. My interpretation is that the lawyers believe that the accounting order does not bind the commission to allow recovery. That is what I always believed and it is the reason I believe the client needs an analysis of the prospects for a favorable recovery rate ruling in the future. One positive is that the costs are being recovered as contributions are made to the trust, not as the benefits are paid to retirees. Thus, it would seem that if the current situation continues, the company's actuary will require an increase in contributions to cover the shortfall. Based on past practice, it seems the commission should allow the recovery of the increased contributions. That is the point we need comfort on based on the company's analysis and advice from rate counsel.

Robert J. Spear



Robert J. Spear
12/30/2002 11:18 AM
617-478-5294
Boston
US

To: Randall J. Vitray/US/ABAS/PwC@Americas-US
cc:
Subject: Re: DTE approval of accounting order

I have asked the Company to pull together an analysis of the probability that interveners will attempt to block recovery in the future rate case. I'll pass along their response when received. Let me know if you want to discuss the materials I sent along re: AG letters and Rate Council's response. Management and Rate Council are available to discuss our questions as needed.

Thanks,
Bob
Randall J. Vitray



Randall J. Vitray
12/26/2002 10:09 AM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc:
Subject: Re: DTE approval of accounting order

I would like to see the letter from the Attorney General. Also, I would like an assessment of the probability that interveners will attempt to block recovery in the future rate case.

<Removed files: Images.TIF>

Robert J. Spear



Robert J. Spear
12/20/2002 06:16 PM
617-478-5294
Boston
US

To: John H McCarthy/US/ABAS/PwC@Americas-US, Simon R. Gerlin/US/ABAS/PwC@Americas-US, Randall J. Vitray/US/ABAS/PwC@Americas-US, Sean P Riley/US/ABAS/PwC@Americas-US
cc:
Subject: DTE approval of accounting order

Attached is the DTE's approval of NSTAR's accounting order for the pension issue along with the DTE's response to the State Attorney General, which had issued a letter opposing the approval. I'll be around Monday afternoon and will try to reach everyone to discuss.

Bob

----- Forwarded by Robert J. Spear/US/ABAS/PwC on 12/20/2002 06:11 PM -----



Fax Server

[BOSPNTADMA01]

12/20/2002 05:43 PM

To: ROBERT J. SPEAR/US/ABAS/PWC@AMERICAS-US

cc:

Subject: A new 5 page fax has arrived from <unknown>

Received on: 2002-12-20 17:40:26
2002-12-20 17:43:52

Processed on:

By fax server:

BOSPNTADMA01 By fax

gateway: BOSPNTADMA01

Number of pages:

5

Duration: 00:02:54



Images.TIF



Randall J. Vitray
12/03/2002 07:31 PM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc: John H McCarthy/US/ABAS/PwC@Americas-US, Sean P
Riley/US/ABAS/PwC@Americas-US, Simon R.
Gerlin/US/ABAS/PwC@Americas-US
Subject: Randy's View - NSTAR Request for Accounting Treatment for Pension
and PBOP

The letter does not provide the support we would need for regulatory asset treatment. I usually view an accounting order as an indicator of the leanings of the regulatory staff, which by itself, would not support a conclusion that recovery in rates is probable. I would want to see a regulatory order granting recovery. If that is not possible, I would want a strong legal opinion from Rate Council that NSTAR has the legal right to recovery and a time line that supports a conclusion that recovery will begin in the near future (i.e. rate case to be filed within months not years).

A negative factor that exists in NSTAR's case is that they have been incurring substantially more pension/OPEB costs than they have been allowed in rates for a long period of time. An analogy to EITF 92-12 seems appropriate.

<Removed files: NOF request comments.pdf>

Robert J. Spear



Robert J. Spear
12/02/2002 11:31 AM
617-478-5294
Boston
US

To: Randall J. Vitray/US/ABAS/PwC@Americas-US
cc: Sean P Riley/US/ABAS/PwC@Americas-US, Simon R.
Gerlin/US/ABAS/PwC@Americas-US, John H
McCarthy/US/ABAS/PwC@Americas-US
Subject: NSTAR Request for Accounting Treatment for Pension and PBOP

Randy:

Attached is a letter that NSTAR sent to the DTE regarding the recovery of all pension costs in rates, including any additional minimum pension liability. The Company is seeking to get regulatory recovery so as to avoid an OCI charge (i.e. establish a regulatory asset). Upon receipt of the letter, the DTE issued a Notice for public comment; a copy of that notice is also attached.

I'd appreciate any thoughts or comments you have on the letter, and whether it's sufficient to allow the Company to record a regulatory asset (assuming of course that the DTE approves the proposal). Let me know if you'd like to arrange a time to talk.

Thanks,
Bob

----- Forwarded by Robert J. Spear/US/ABAS/PwC on 12/02/2002 11:18 AM -----



"Weafer, Robert"
<Robert_Weafer@nstar
online.com>
12/02/2002 06:39 AM

To: Robert J. Spear/US/ABAS/PwC@Americas-US, Sean P
Riley/US/ABAS/PwC@Americas-US, "DelMonte, Daniel"
<Daniel_DelMonte@nstaronline.com>, "Moreira, John"
<John_Moreira@nstaronline.com>, "Landry, Leanne"
<Leanne_Landry@nstaronline.com>
cc:
Subject: FW: 02-78 NSTAR Request for Accounting Treatment for Pension and
PBOP

Fyi,

Bob


> -----Original Message-----
> From: Ly, Tam
> Sent: Friday, November 29, 2002 10:14 AM
> To: Weafer, Robert; Judge, James; Farrell, Michael; Robert N. Werlin
> (E-mail); Cheryl Kimball (E-mail); Kimball, Cheryl; Rabadjiya, Neven;
> Morrison, Richard; Lanzel, Joseph; LaMontagne, Henry; Lubbock, Geoffrey
> Cc: Eliezer Velez (E-mail)
> Subject: 02-78 NSTAR Request for Accounting Treatment for Pension
and
> PBOP
>
> Folks,
>
> Attached below is a DTE Notice and Request for Comments regarding the
> Company's request in the above-referenced matter.
>
> Tam
>
> <<NOF request comments.pdf>>

This email and any files transmitted with it are confidential and
intended solely for the use of the individual or entity to whom they
are addressed. If you have received this email in error please notify
the system manager.

Client Name: NSTAR
Period End: 12/31/2002

Critical Matter

Title: Accounting for the 12/31/2002 Minimum Pension Liability Regulatory Asset - FINAL

Parent Link:  12/31/02 Consolidated Reg Assets Flux

Area: 3250 -Deferred Debits
File Section: Other audit evidence - Assets

Related Areas:

Type:
Significant accounting or auditing or reporting matter
Critical Matter = Yes
Point Forward = No

Client Site:


Clearance Required = Yes

Description:

Background

As a result of the significant decrease in the fair value of the Company's defined benefit pension plan assets due to continued market losses in 2002, as well as changes in the benchmark interest rates (used for purposes of selecting a discount rate as of 12/31/2002 for liability measurement purposes), the Company was required to record a minimum pension liability adjustment as of 12/31/2002. This minimum liability adjustment is required by SFAS 87 paragraph 36 as follows:

If the accumulated benefit obligation exceeds the fair value of plan assets, the employer shall recognize in the statement of financial position a liability (including unfunded accrued pension cost) that is at least equal to the unfunded accumulated benefit obligation. Recognition of an additional minimum liability is required if an unfunded accumulated benefit obligation exists and (a) an asset has been recognized as prepaid pension cost, (b) the liability already recognized as unfunded accrued pension cost is less than the unfunded accumulated benefit obligation, or (c) no accrued or prepaid pension cost has been recognized.

NSTAR had been in a prepaid pension position as of December 31, 2001 of \$218.7 million. As of the December 31, 2002, the Company continued to remain in a prepaid position of \$257 million. However, due to the market factors discussed above, the accumulated benefit obligation (ABO) was in an underfunded position (ABO at \$844 million vs Fair Value of Assets at \$666 million) - requiring the Company to record an additional minimum liability of \$178 million. (Refer to wp 4800-2  - Pension for testing relating to the minimum liability).

Issue

In accordance with SFAS 87, when recording a minimum pension liability adjustment (credit to "Deferred Credits"), NSTAR would be required to post the offset (debit) to "Other Comprehensive Income" (on a net of tax basis) in accordance with SFAS 87 paragraph 37. (Note that NSTAR booked an intangible asset adjustment of \$980k - see paragraph 36 of SFAS 87). Due to the significant negative impact that a minimum liability charge would have on the equity of NSTAR, management has sought alternative accounting under SFAS 71. At issue is the following:

- (1) Could NSTAR theoretically be allowed to record the debit associated with the recognition of a

minimum liability to a regulatory asset account rather than OCI, if such a debit qualifies under paragraph 9 of SFAS 71? In other words, could a charge to equity meet the definition under SFAS 71 as an "incurred cost that would otherwise be charged to expense"?

- (2) If the answer to (1) above is "yes", what must NSTAR do to support the recognition of the regulatory asset.

Discussion and Conclusion

Question 1:

SFAS 71 "Accounting for the Effects of Certain Types of Regulation" paragraphs 5 and 9 provide the definitive guidance related to the recognition of regulatory assets. Specifically, paragraph 9 states the following:

Rate actions of a regulator can provide reasonable assurance of the existence of an asset. An enterprise shall capitalize all or part of an incurred cost (defined as a cost arising from cash paid out or obligation to pay for an acquired asset or service, a loss from any cause that has been sustained and has been or must be paid for" (Eric L. Kohler, A Dictionary for Accountants, 5th ed. [Englewood Cliffs, N.J.: Prentice-Hall, Inc., 1975], p. 253)) that would otherwise be charged to expense if both of the following criteria are met: (a.) It is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes; and (b.) Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs. If the revenue will be provided through an automatic rate-adjustment clause, this criterion requires that the regulator's intent clearly be to permit recovery of the previously incurred cost.

The PwC team consulted with Casey Herman (PwC Partner and Utility Industry Technical Liason) and Randy Vitray to assess whether a charge to OCI as a result of a minimum liability adjustment could meet the definition of "an incurred cost". Casey indicated that he (in conjunction with Paul Keglevic, PwC Utility Industry Leader) believed that a charge to OCI for a minimum liability adjustment did qualify as an "incurred cost". Casey noted that SFAS 71 was issued well before the concept of comprehensive income was introduced in SFAS 130 - and 71 should have been amended to address this type of issue. Ultimately, the charge to OCI would reverse through the income statement and therefore, if the regulator was allowing full recovery of the all pension costs (under a SFAS 87 basis), and the charge qualified under requirement 9(a) and 9(b) of SFAS 71, a regulatory asset could be established.

Randy Vitray, PwC National R&Q partner agreed with Casey's conclusion - and added that precedent exists relating to recording other adjustments as a regulatory asset or liability that would typically be recorded as an adjustment to OCI. For example, some regulators have required that all gains / losses related to interest rate SWAPs be returned to / recovered from ratepayers. As a result, rather than recording an OCI charge for the change in the FV of an interest rate SWAP as would be required for a cash flow hedge, the debit or credit gets reported as a regulatory asset or liability. In addition, Randy also pointed to EITF D-41 (which addresses SFAS 115 related OCI adjustments for Holding Gains / Losses). Ultimately, Randy concluded that precedent exists for being able to record the minimum liability adjustment offset to regulatory assets - assuming the criteria under paragraph 9(a) and (b) of SFAS 71 are met.

Question 2:

The engagement team instructed NSTAR management that the criteria of SFAS 71 (paragraph 9(a) and (b)) and EITF 99-12 would need to be met in order to record a regulatory asset rather than charge OCI. Stated briefly, the criteria to be satisfied involved: a rate order from the regulator allowing recovery or a conclusion that recovery of amounts is probable (which involves a legal determination) and the ability and

commitment of the Company to file a rate case as soon as practicable to effect recovery. To meet this criteria, NSTAR provided the following to PwC:

- a) An accounting order from the DTE allowing NSTAR to record the debit for the minimum liability charge as a regulatory asset;
- b) An opinion from external rate counsel that stated that based on the language of the accounting order, the Company had the legal right to recover the regulatory asset, and that it was probable of recovery; and
- c) A representation to PwC that management believed the regulatory asset was probable of recovery.

The engagement team's conclusion based on the above evidence is that it is appropriate and reasonable to recognize the difference between the amount collected in rates and the actual SFAS 87 / 106 cost as a regulatory asset or liability, and to defer as a regulatory asset the amount of Additional Minimum Liability at 12/31/2002 to reflect the Company's ability to recover in rates over time its actual pension liability. PwC considered the accounting order received from the DTE as strong, but not definitive, evidence of the Commission's intent related to recovering pension and post-retirement costs as recognized under SFAS 87 and 106. However, the order, supported by external rate counsel and management's representation related to the probability of recovery of such costs does allow the Company to meet the criteria under paragraph 9(a) and (b) of SFAS 71 - and therefore, recognition of the regulatory assets of \$426 million as of 12/31/2002 is appropriate. This issue was reviewed with Randy Vitray - who agreed with the engagement team's conclusion.


The details of the nature and amount of the minimum liability adjustment, SFAS 87 / 106 expense, and associated regulatory assets will be fully disclosed in the Company's annual report and Form 10-K for 2002.

ATTACHMENTS



a) Accounting order received from the DTE: Images.TIF Key points to note are as follows:

- Order was unanimously approved by the DTE on 11/27/2002
- The order allows NSTAR to defer the difference between the amount collected in rates and the actual SFAS 87 / 106 cost as a regulatory asset or liability, and to defer as a regulatory asset the amount of its current and future Additional Minimum Liability to reflect the Company's ability to recover in rates over time its actual pension liability.

b) The key points of the rate counsel opinion (Keegan & Werlin) is as follows (see external wp 4800-15  for the signed letter):

- The opinion addresses the legal right of the Company to recover its SFAS 87 costs, as well as the probability of future recovery of the amounts the DTE has permitted NSTAR to defer under its accounting order;
- It is rate counsel's opinion that the accounting ruling that permits the deferral of costs will result in the subsequent reconciliation and recovery of such prudently incurred costs. Accordingly, based on the Department's approval of the request for an accounting ruling, counsel is of the opinion that it is probable that the Department will approve a reconciling mechanism that will permit recovery of pension and post-retirement costs that have been deferred in accordance with the Department's accounting order.

c) The language to be included in the 2002 representation letter associated with the minimum liability regulatory asset is as follows:

"On November 27, 2002, the Company filed a request for an accounting order with the MDTE to authorize an accounting practice whereby the Company would be allowed, unless otherwise ordered by the MDTE, to defer, and record as a regulatory asset, the amount of its current and future additional minimum pension liability to reflect the Company's ability to recover these costs in rates over time. The request further specified that a specific recovery mechanism to recover the deferred pension costs would be proposed in an upcoming rate case proceeding. On December 20, 2002, the MDTE approved the request. In connection with the MDTE's approval of the accounting order, the Company has conducted an analysis of its legal right to recovery and of the prospects of a favorable recovery rate ruling in the future. In addition, as part of that analysis, the Company has also considered the potential impact of those parties who may seek to intervene to block recovery in the future rate case. Based on our analysis, we represent that future recovery of the regulatory asset created at December 31, 2002 attributable to the pension costs deferred as a result of the MDTE's approval of the aforementioned accounting order is probable. We further represent that our plan is to file a rate case with the MDTE in the second quarter of 2003 which will include a specific mechanism designed to recover the pension costs that have been deferred as of December 31, 2002."

This representation meets PwC's requirements, as management has represented:

- that they believe the order reflects the Company's ability to fully recover its SFAS 87 expenses (costs) over time;
- that they will file for a rate case in early 2003, therefore the specific recovery mechanism will be established in 2003 to recover such costs going forward;
- that they believe the potential for a third party attempt to prevent full recovery is not significant, and recovery of all SFAS 87 costs remains probable.

d) Copies of various email correspondence associated with the engagement team consultation with PwC-National:

Randall J. Vitray
12/31/2002 01:25 PM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc: Sean P Riley/US/ABAS/PwC@Americas-US
Subject: Re: DTE approval of accounting order

Sounds good to me.

This also sounds like a good precedent for the industry. Can you forward this to Casey Herman for that purpose?

Robert J. Spear

Robert J. Spear
12/31/2002 11:48 AM
617-478-5294
Boston
US

To: Randall J. Vitray/US/ABAS/PwC@Americas-US
cc: Sean P Riley/US/ABAS/PwC@Americas-US
Subject: Re: DTE approval of accounting order

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Management is prepared to provide the representations we need regarding these points (up to the CEO level). Rate Council believes it has provided a strongly worded opinion, but they are open to discussions of any other wording we may need. Also, a plan has been put in place for the Company to file for a rate case by mid-March/April (the timing of our audit of the FERC Form 1s has been accelerated to facilitate this filing date).

I believe we have the support we need. Let me know what you think.

Thanks,
Bob

Randall J. Vitray


Randall J. Vitray
12/30/2002 05:02 PM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc:
Subject: Re: DTE approval of accounting order 

I looked at the material. My interpretation is that the lawyers believe that the accounting order does not bind the commission to allow recovery. That is what I always believed and it is the reason I believe the client needs an analysis of the prospects for a favorable recovery rate ruling in the future. One positive is that the costs are being recovered as contributions are made to the trust, not as the benefits are paid to retirees. Thus, it would seem that if the current situation continues, the company's actuary will require an increase in contributions to cover the shortfall. Based on past practice, it seems the commission should allow the recovery of the increased contributions. That is the point we need comfort on based on the company's analysis and advice from rate counsel.

Robert J. Spear

Robert J. Spear
12/30/2002 11:18 AM
617-478-5294
Boston
US

To: Randall J. Vitray/US/ABAS/PwC@Americas-US
cc:
Subject: Re: DTE approval of accounting order 

I have asked the Company to pull together an analysis of the probability that interveners will attempt to block recovery in the future rate case. I'll pass along their response when received. Let me know if you want to discuss the materials I sent along re: AG letters and Rate Council's response. Management and Rate Council are available to discuss our questions as needed.

Thanks,
Bob



AG Comments 02-78.p



02-78 NSTAR Response to AG Comments (12-17-02)



AG Reply Comments 02-78.r

Randall J. Vitray

Randall J. Vitray
12/26/2002 10:09 AM

To: Robert J. Spear/US/ABAS/PwC@Americas-US
cc:
Subject: Re: DTE approval of accounting order

I would like to see the letter from the Attorney General. Also, I would like an assessment of the probability that interveners will attempt to block recovery in the future rate case.

Robert J. Spear

Robert J. Spear
12/20/2002 06:16 PM
617-478-5294
Boston
US

To: John H McCarthy/US/ABAS/PwC@Americas-US, Simon R. Gerlin/US/ABAS/PwC@Americas-US, Randall J. Vitray/US/ABAS/PwC@Americas-US, Sean P Riley/US/ABAS/PwC@Americas-US
cc:
Subject: DTE approval of accounting order

Attached is the DTE's approval of NSTAR's accounting order for the pension issue along with the DTE's response to the State Attorney General, which had issued a letter opposing the approval. I'll be around Monday afternoon and will try to reach everyone to discuss.

Bob

----- Forwarded by Robert J. Spear/US/ABAS/PwC on 12/20/2002 06:11 PM -----

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12/20/2002 05:43 PM

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Reviewed By: John H McCarthy	Date: 05/21/2003
Cleared By: Robert J. Spear	Date: 05/21/2003
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Maintenance

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Last Modified By: Robert J. Spear	Date: 05/21/2003
Editors: Sean P Riley; John S. Miele; John H McCarthy; Robert J. Spear	

**NSTAR**

800 Boylston Street, Boston, Massachusetts 02119-8003

D.T.E. 02-78

James J. Judge

Senior Vice President, Chief Financial Officer and Treasurer

November 27, 2002

Paul B. Vasington, Chairman
 James Connelly, Commissioner
 W. Robert Keating, Commissioner
 Eugene J. Sullivan, Jr., Commissioner
 Deirdre K. Manning, Commissioner
 Department of Telecommunications and Energy
 One South Station - 2nd Floor
 Boston, Massachusetts 02110

APPROVED	
DATE	<i>Paul B. Vasington</i>
	<i>James Connelly</i>
	<i>W. Robert Keating</i>
	<i>Eugene J. Sullivan Jr. (OK)</i>
	<i>Deirdre K. Manning</i>
COMMISSIONERS, D.T.E.	

Re: Accounting Treatment for Pension and Post-Retirement Benefits

Dear Commissioners:

Since 2000, the U.S. economy has experienced three consecutive years of significant equity-market declines coupled with falling interest rates. This unprecedented occurrence is having a considerable impact on NSTAR's obligations regarding employee pensions and post-retirement benefits other than pensions ("PBOP").¹ Consequently, by this letter, I am seeking the assistance of the Department of Telecommunications and Energy (the "Department") in mitigating the negative effects of certain accounting and ratemaking requirements that are implicated as a result of these unprecedented economic circumstances.

Over the past 10 years, NSTAR² has contributed an average of approximately \$85 million per year into its trust funds specially established to hold and invest funds designated to pay pensions and PBOPs to retired employees. Over that same time period, the amount of pension and PBOP costs embedded in rates averaged only approximately \$47 million per year. In accordance with Department policy, NSTAR has consistently made significant annual contributions to the pension and PBOP trust funds well in excess of the minimum levels required by the Employee Retirement Income Security Act of 1974 ("ERISA") and Internal Revenue Service ("IRS") regulations. Although this level of contribution greatly exceeded the level of expenses previously included in approved utility rates, NSTAR's funding policies ensured that trust funds were tax efficient and adequately funded so that benefits would be available to be paid to employees upon retirement.

¹ There are two accounting standards that have been issued by the Financial Accounting Standards Board ("FASB" or the "Board") that are germane to the Company's funding obligations for pensions and PBOPs. These standards are the Statement of Financial Accounting Standards No. 87 ("FAS 87") and No. 106 ("FAS 106"), which govern accounting practices for pension and PBOP expenses, respectively. The Board issued FASB 87 (Pensions) in December 1985 (effective in 1987) and FASB 106 (PBOPs) in December 1990 (effective in 1993).

² For purposes of this letter, "NSTAR" or the "Company" refers to its regulated operating utilities, Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company.

Letter to Commissioners

November 27, 2002

Page 2

Despite these substantial contributions, NSTAR is now confronted with a serious accounting deficiency in its pension fund resulting from equity-market declines and falling interest rates. In combination, these factors have the dual impact of reducing the value of the assets held in trust to meet pension obligations, while at the same time increasing the benefit obligation (because a lower interest rate increases the present value of the benefit obligation to employees in the future).

Absent an accounting ruling from the Department, this shortfall will require NSTAR to record on its books a large non-cash charge to Other Comprehensive Income/Loss ("OCI"). Although the charge to OCI would be reversed in future periods, this charge to common equity would have an immediate and detrimental effect on NSTAR's financial health, and ultimately, the cost of service for NSTAR customers. For example, the Company's bond ratings are likely to be downgraded, which will increase the costs that the Company will incur to raise capital and finance utility operations. In addition, the Company's credit agreements may be negatively affected by this downgrading, which could further impair the Company's access to capital to continue financing system improvements and fund utility operations. The Company also anticipates that the situation would create concerns among employees and customers.

In addition, the expenses that will be booked under FAS 87 and FAS 106 in 2003 and forward will be significantly greater than the levels previously booked by the Company. Moreover, because changes in the position of the trust funds resulting from market volatility are captured in the IRS calculation of tax deductibility for fund contributions, the maximum for pension funds in 2003 is projected to be substantially greater than the \$50 million per year that the Company has invested in the pension fund on average over the past five years.

The Department has consistently recognized that prudently incurred pension and PBOP costs may be included in utility rates. Given the volatility of these extraordinary and recurring expenses (whether viewed in terms of FAS 87 and FAS 106 expenses or tax deductible contributions), the Company will propose in a future proceeding a specific recovery mechanism designed to provide for the reconciliation between the amounts received from customers in rates and the FAS 87 and FAS 106 expenses recorded on the Company's books over a specified time period.³ The approval of such a mechanism will ensure that the Company's customers pay in rates no more than the Company's actual pension liability, and the Company will collect only the actual amount of its actual pension obligation. Such a reconciliation is consistent with the Department's rate-continuity principles in that it will stabilize and smooth out the recovery of the

³ Such treatment has been approved in similar circumstances by the Department in the past. See e.g., Boston Gas Company, D.P.U. 93-60, at 207-208 (1993); Boston Edison Company, D.P.U./D.T.E. 96-23 (1998) (approving Restructuring Settlement Agreement that provides that "post divestiture FAS 106 and FAS 87 gains or losses recognized on BECo's books shall be reflected in distribution rates to customers and shall neither be retained nor borne by BECo." Restructuring Settlement, at page 233, fn.5); Cambridge Electric Light Company, D.P.U. 92-250, at 54 (1993); Manufactured Gas Waste Generic Investigation, D.P.U. 89-161 (1990).

Letter to Commissioners
November 27, 2002
Page 3

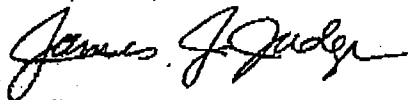
expense from customers, while avoiding adverse financial impacts. Without the approval of such a mechanism the volatility of pension expense and funding requirements, combined with the magnitude of these amounts, will significantly distort the annual reporting of the Company's operating results in the future and could result in the over-collection of costs from customers.

To avoid this result as well as the immediate and detrimental impacts associated with the year-end charge to equity of the Additional Minimum Liability ("AML"),⁴ the Company requires an accounting ruling from the Department on or before December 31, 2002, that would permit, pending the establishment of the specific ratemaking methodology to reconcile and to recover costs, the deferral of the difference between the level of pension and PBOP expenses that are included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106, in recognition of the recoverability of these costs in future rates, as determined by the Department in the Company's next rate proceeding. Accordingly, the Company requests that it be authorized to implement the following accounting practices:

- (a) until otherwise ordered by the Department, the Company will defer, and record as a regulatory asset or liability, the difference between the level of the pension and PBOP expenses that are included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106; and
- (b) until otherwise ordered by the Department, the Company will defer as a regulatory asset the amount of its current and future Additional Minimum Liability to reflect the Company's ability to recover in rates over time its actual pension liability.

Thank you for your attention and consideration of this request.

Sincerely,



James J. Judge
Senior Vice President,
Treasurer and Chief Financial Officer

cc: Joseph Rogers, Assistant Attorney General
Paul Afonso, General Counsel
Kevin Brannelly, Director, Division of Rates and Revenue Requirements

⁴ The AML represents the amount by which the Company's pension plan obligations exceed the value of the assets in the trust fund at the end of each calendar year.



JANE SWIFT
GOVERNOR

JENNIFER DAVIS CAREY
DIRECTOR OF CONSUMER AFFAIRS
AND BUSINESS REGULATION

THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF CONSUMER AFFAIRS AND BUSINESS REGULATION

DEPARTMENT OF
TELECOMMUNICATIONS & ENERGY

ONE SOUTH STATION

Boston, MA 02110
(617) 305-3500

PAUL B. VASINGTON
CHAIRMAN

JAMES CONNELLY, ESQ.
COMMISSIONER

W. ROBERT KEATING
COMMISSIONER

EUGENE J. SULLIVAN, JR.
COMMISSIONER

DEIRDRE K. MANNING
COMMISSIONER

December 20, 2002

Joseph W. Rogers
Assistant Attorney General
Office of the Attorney General
200 Portland Street
Boston, Massachusetts 02114

Re: NSTAR Electric/NSTAR Gas Company, D.T.E. 02-78

Dear Mr. Rogers:

Enclosed please find the approval of the Department of Telecommunications and Energy ("Department") concerning the request by Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company ("NSTAR" or "Company") (1) to defer, and record as a regulatory asset or liability, the difference between the level of the pension and post-retirement benefits other than pensions ("PBOP") expenses that are included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106, and (2) to defer as a regulatory asset the amount of its current and future Additional Minimum Liability to reflect the Company's ability to recover in rates over time its actual pension liability.

In evaluating the Company's petition for an accounting ruling, the Department carefully considered the issues raised by the Attorney General in his comments submitted on December 13, 2002 as well as December 19, 2002 and acknowledges his request that the Department conduct a proceeding to investigate issues relating to the Company's requested accounting treatment. Because the Department's approval of the Company's request does not

FAX: (617) 345-9101 TTY: (800) 323-3298

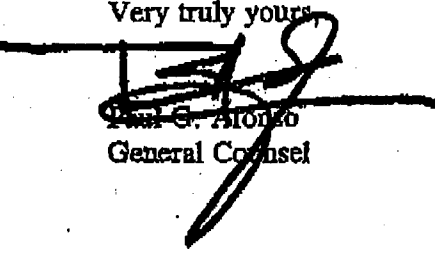
www.mass.gov/dtu

D.T.E. 02-78

Page 2

predetermine the mechanism for establishing the amount of pension and PBOP costs that would be included in rates, the Attorney General's right to investigate this matter, which would include discovery and hearings, in NSTAR's next rate proceeding, when the amount of pension and PBOP costs would be determined, is not affected by the Department's ruling in this matter.

Very truly yours,


Paul G. Aronoff
General Counsel

cc: Commission
Mary L. Cottrell, Secretary
Caroline O'Brien, Hearing Officer
Robert J. Keegan, Esq.



THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF THE ATTORNEY GENERAL

200 PORTLAND STREET
BOSTON, MASSACHUSETTS 02114

TOM REILLY
ATTORNEY GENERAL

(617) 727-2200
<http://www.ago.state.ma.us>

SENT ELECTRONICALLY, BY FAX AND MAIL

December 12, 2002

Mary Cottrell, Secretary
Department of Telecommunications and Energy
One South Station, 2nd Floor
Boston, MA 02110

RE: Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company, D.T.E. 02-78

Dear Secretary Cottrell:

On November 27, 2002, the Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company ("NSTAR" or Company") filed a request with the Department of Telecommunications and Energy ("Department") for an accounting deferral related to pension and post-retirement benefits other than pensions ("PBOP"). On the same day, the Department issued a Notice of Inquiry that set December 9, 2002, as the deadline for submitting comments on the Company's filing, which has been extended until today. Since the Company has not demonstrated a *prima facie* case entitling it to the deferral, the Department should either deny the petition outright or at least allow discovery and conduct an evidentiary hearing on the petition prior to ruling on the request. *North Attleboro Gas Company*, D.P.U. 93-229, p. 7 (1993).

Generally Accepted Accounting Principles ("GAAP") require the Company to record on its financial statements (1) its expected liabilities associated with its pension plan and PBOP, and (2) the assets associated with their respective trust funds. Pension accruals booked each year vary and are somewhat subjective; they involve actuarial expectations of the returns on the trust funds, the rise in health care costs, the mortality of the employees, and the expected discount rate. All of these assumptions change over time, and therefore, the Company's pension and PBOP liabilities change over time. The annual pension liability changes flow through to the Company's bottom line and affect its reported earnings from year to year. These changes, however, may have little or no effect on the actual cash flow or out-of-pocket costs that the Company will incur in any given year. The Company proposes that the Department, until it may

otherwise order, allow the Company to: (a) defer, and record as a regulatory asset or liability, the difference between the level of the pension and PBOP expenses that are included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106; and (b) defer as a regulatory asset the amount of its current and future Additional Minimum Liability to reflect the Company's ability to recover in rates over time its actual pension liability.

The Department has a clear standard for reviewing petitions, such as the one NSTAR filed here, for deferral accounting treatment. *North Attleboro Gas Company*, D.P.U. 93-229, p. 7-8 (1994).¹ A company must make a *prima facie* showing in its petition that: (1) the expense would be recoverable under Department precedent if it were incurred during a test year; (2) denying the deferral would significantly harm the company's overall financial condition; and (3) denying the deferral is likely to cause the filing of a rate case that includes in the test year the expense for which deferral is sought. NSTAR has not met any of these three elements of the *prima facie* test. Neither the booked expense amount nor the Additional Minimum Liability are recoverable under Department precedent. *Fitchburg Gas and Electric Light Company*, D.T.E. 02-24 / 02-25, pp. 111, 115 (2002) ("[t]he Department's general policy with respect to pension expense is to limit rate recovery to test year cash contributions to the pension plan because accrual-based pension cost estimates generally cannot be shown to be annually or periodically recurring.") ("[t]he Department has found that the actual cash contribution to a tax-deductible trust strikes a balance of interests between shareholders and ratepayers") The Company has not demonstrated with any facts that, even with a write-off of equity, its bond ratings actually will be reduced or that any such reduction would significantly harm NSTAR's strong overall financial condition or harm ratepayers more than the additional costs associated with the requested deferrals.² Finally, denying the deferral will not cause a rate case; the Company told the Attorney General that it intended to file rate cases in 2003 months before this issue even arose.

Once a *prima facie* showing is made, the Department will evaluate the petition, considering such additional factors as: (a) the company's ability to choose a test year; (b) the company's history and frequency of rate increases; (c) the company's frequency of requests for deferrals; (d) the company's earnings in the year the subject expense was incurred; and (e) whether some voluntary agreement on the part of the petitioner (e.g., a settlement) would otherwise preclude bringing a rate case during the period for which deferral is sought. Granting a deferral does not guarantee recovery of the subject expense in a future rate case. Rather, subsequent ratemaking treatment of the expense would be considered in the company's next rate case. Regarding these additional factors, the Company may elect to file a rate case as early as March of 2003 for effect after the expiration of the four year merger "rate freeze" period.

¹ The Department's policy behind granting deferrals is based in administrative efficiency: to avoid unnecessary rate cases which would be triggered by certain extraordinary pretest year expenses.

² To the contrary, NSTAR's strong "A" bond ratings have not dropped even after the Company announced in November, 2002, the expected effects on its balance sheet of the pension and PBOP accounting.

NSTAR reported earnings of 12.1 percent for 2001, and the consensus forecast for 2002 is for similar strong earnings.

The Company's request also raises questions under the Department ordered "rate freeze" associated with the NSTAR merger. *BEC Energy / ComEnergy*, D.T.E. 99-19, pp. 5, 25, 85 (1999).³ According to Department precedent, a utility may not defer a cost during the period covered by a rate settlement that fixes rates unless specifically allowed by the terms of the agreement. *North Attleboro Gas*, D.P.U. 93-229, p. 6 (1993) (denial of deferral request since expense occurred during period of settlement and expense did not qualify as an exogenous cost). Through the settlement, a company's election to limit its rates for a number of years also "forecloses its ability to file for and therefore recover rates beyond those specified" in the agreement. *Id.* It now appears that NSTAR seeks ongoing accounting deferrals for periods covered by the freeze and beyond.

Therefore, NSTAR has failed to establish a *prima facie* case. The Department should either deny the petition outright or at least hold a hearing on the Company's proposal for the following reasons:

- (1) The Company has not established that the "true-up" amount is an extraordinary operating expense that Department precedent would allow as proper for deferral, *Boston Gas Company*, D.P.U. 89-177, pp. 7-8 (1989), or that the costs are recoverable from customers in a subsequent rate case.
- (2) The Company has not established the level of pension and PBOP expenses in the Company's rates. The relevant rates of the distribution companies were fixed by settlement or rate cases that are as much as ten years old.⁴ Several of the NSTAR companies rates were set in settlements; in the settled rate cases there are no Department findings on the specific dollar amounts of individual costs, including pension and PBOPs.
- (3) The Company has not established that the pension and PBOP expenses cannot be changed from year to year simply by making minor changes in actuarial assumptions, thus directly affecting the regulatory asset balance.
- (4) The Company has not established that any of the individual distribution companies will

³ The Attorney General has appealed the merger decisions in *BEC Energy / ComEnergy*, D.T.E. 99-19 (1999) and frames his arguments, as he must, in this case with the understanding that the Department's order is in effect until modified or overturned by the Massachusetts Supreme Judicial Court. As the appeal is still pending, nothing in these comments should be construed as an adverse admission or waiver of any legal or factual argument that the Attorney General has made in the pending appeal.

⁴ The Company's kilowatt-hour sales have increased by 19 percent in the last ten years; revenues being collected through rates are therefore higher than the amounts found in those cases.

experience severe detrimental financial effects without the proposed deferral. In fact, NSTAR reported to the financial community an estimated \$200 – \$300 million impact of this accounting at end of the third quarter, yet the Company's bond rating has not changed, and the evidence does not show that the Company is having difficulty attracting capital. This transaction is not a cash outlay, rather it is an accounting accrual apparently recorded by the holding company.

- (5) The Company has not established the actual amount of the deferral and references stale data. The Company accounted for its pension and PBOPs trust fund assets for the most recently reported quarter, September 30, 2002. Since that time the stock market has risen 18 percent. The Company has failed to indicate what the expected deferral amount will be by December 31, 2002.
- (6) The Company indicated that this accounting problem is for the year 2002 and the situation will reverse in 2003. The Company, however, has not indicated what the Department should do if the situation reverses itself in 2003.

While the Attorney General is concerned about NSTAR's allegations that denial of the petition could lead to detrimental financial consequences that may harm customers, the Company has not shown that such consequences will in fact result notwithstanding NSTAR's strong financial position overall. The Company has made a number of statements that require further examination, discovery and briefing. Since NSTAR failed to provide a sufficient factual basis to support its proposed calculations and the requested deferral, the Department should either deny the petition outright or at least allow discovery and conduct a hearing to fully examine the issues and determine the facts before ruling on the request.

Sincerely,

Joseph W. Rogers
Division Chief
Utilities Division

cc: Service list

Workpaper 4800-2

NSTAR
Additional Minimum Liability
12/31/2002

Prepaid= \$257,015,443.16
Plan Assets= \$665,897,000
ABO= \$843,572,000 *WW*
Unfunded ABO= (\$177,675,000)

Acct. #	Description	RECO	ComElectric	Cambridge	NSTAR Gas	NE&G	Parent	Consolidated
		60.64%	17.00%	2.51%	18.02%		1.83%	100.00%
146300	Rec. fr. NE&G	171,094,158						
182XXX (New Account)	Pension AML Reg. Asset	5,600,842						
186020	Intangible asset	980,000						
254010	Pension liability	(177,675,000)						
146150	Rec. fr. ComElectric					73,897,375		
146160	Rec. fr. CEL					10,910,730		
146200	Rec. fr. NSTAR Gas					78,331,218		
146002	Rec. fr. Parent					7,954,835		
234120	Pay. To RECO					(171,094,158)		
182XXX (New Account)	Pension AML Reg. Asset		73,897,375	10,910,730	78,331,218		4,834,551	
234300	Pay. To NE&G		(73,897,375)	(10,910,730)	(78,331,218)		2,603,220	
216750	Other Comp. Income						517,084	
283010	Fed. ADIT						(7,954,835)	
283020	Mass. ADIT							
234300	Pay. To NE&G							
Ending Balances								
Pension AML Reg. Asset								168,740,165
Prepaid reg. Asset								257,015,443
Intangible asset								980,000
OCI								4,834,551
ADIT								3,120,284
Check								434,690,443
Prepaid								257,015,443
Unfunded ABO								177,675,000
								434,690,443

KEEGAN, WERLIN & PABIAN, LLP

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BOSTON, MASSACHUSETTS 02110-3525

(617) 951-1400

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(617) 951-1354
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December 17, 2002

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station
Boston, Massachusetts 02110

Re: NSTAR Electric Company/NSTAR Gas Company, D.T.E. 02-78, Response of
NSTAR to Comments of the Attorney General

Dear Secretary Cottrell:

On December 13, 2002, the Attorney General filed comments with the Department of Telecommunications and Energy (the "Department") concerning the November 27, 2002 request filed by Boston Edison Company, Cambridge Electric Light Company and Commonwealth Electric Company and NSTAR Gas Company (collectively "NSTAR" or the "Company") for an accounting ruling relating to pension and post-retirement benefits other than pensions ("PBOP"). NSTAR hereby files a response to the Attorney General.

In his comments, the Attorney General requests that the Department either deny the Company's request or allow for discovery and an evidentiary hearing to "fully examine the issues" prior to ruling on the request (Attorney General Comments at 1, 4). The Attorney General's recommendations are based solely on the claim that, under Department precedent, there is a "clear standard" that applies to the Company's requested accounting treatment and that, under this standard, the Company has "not demonstrated a prima facie case entitling it to a deferral" (id. at 2). As discussed below, the Attorney General's claim is flawed in that it misconstrues the nature and effect of the Company's request and rests on a misapplication of Department precedent.

As an initial matter, however, the Company would like to address the Attorney General's assertion that, although the denial of the Company's request could lead to detrimental financial consequences that may harm customers, the Department should deny the request or delay a ruling on the request because the Company has not shown that detrimental financial consequences "will in fact result" from a denial of the request (id. at 4).¹ The Attorney General's standard would effectively place customers at a

¹ In this case, a delay by the Department in ruling on the request to allow for discovery and an evidentiary hearing is tantamount to a denial since the accounting entries must be made as of December 31, 2002.

significant risk of incurring increased costs of capital in the future, without any potential benefits or protections to offset that risk. It is widely recognized by credit rating agencies that a reduction in book equity will result in a higher debt-to-capital ratio, which, in turn, has negative implications on a company's ratings, and ultimately, the cost of borrowings. Attached is a September 12, 2002 article by FitchRatings, which discusses the impact of pension accounting on a company's financial health. Consistent with the statements made therein, a \$200-\$300 million charge against equity will significantly weaken the Company's balance sheet and reduce common equity by approximately 20 percent. The Attorney General does not dispute this fact, but rather claims that this type of significant reduction will not result in detrimental financial consequences for the Company. The Attorney General's assertion has no basis in fact and misrepresents the historical impact of this type of change in a company's capital ratios.

The Company routinely confers with the rating agencies and possesses the experience and expertise to know that, in the absence of the accounting ruling, the Company's bond rating will be immediately called into question. As the Department is aware, the Company recently received approval and intends to issue long-term debt of up to \$150 million for Commonwealth Electric Company. See, Commonwealth Electric Company, D.T.E. 02-51 (2002). The issuance of debt securities in the face of an impaired debt-to-equity ratio, will inevitably result in the debt being issued at a higher cost than without the equity charge. Moreover, the Company routinely relies on significant short-term debt instruments to fund day-to-day operations. These transactions will also be more costly as a result of the changed equity status of the Company. Therefore, denial of the accounting ruling has the potential to dramatically increase the Company's cost of capital and to increase the cost of service borne by customers. Thus, the Attorney General's argument that denial of the accounting ruling will have no negative impact on the Company or its customers is unfounded and erroneous and should be rejected by the Department.

In fact, because no change in rates would be instituted upon the Department's approval of the Company's request, customers can only be harmed by the denial or delay in the approval of the request. The Department's approval of the accounting treatment requested by the Company would preclude the unavoidable year-end accounting adjustments required of the Company, and therefore, eliminate entirely the potential for any detrimental financial consequences that would result in harm to customers. At the same time, as acknowledged in the Company's request, the Department's approval would leave open the underlying issues relating to the specific ratemaking methodology that would be used to recover pension and PBOP-related costs in the future. Therefore, as stated above, a decision by the Department to grant the accounting treatment would protect customers from the detrimental effects of the year-end accounting requirements, while preserving the Attorney General's ability to participate on behalf of customers in a future proceeding to establish the specifics of the cost-recovery mechanism before any

change in rates is implemented.² Because customers have significant exposure if the request is denied or delayed, the Department should reject the Attorney General's request to deny or delay the request on the basis that the financial impact of a charge to equity of this magnitude cannot be precisely quantified.

In addition to understating the seriousness of the detrimental financial consequences that would result from a write-off, the Attorney General has applied a standard of review that is inapplicable to the Company's request. As discussed in detail below, the issues driving the Company's request are a function of unprecedented economic circumstances coupled with the constraints of the financial accounting and ratemaking processes, which have not previously been considered by the Department. As a result, the Attorney General's attempt to assert that any and all requests for accounting treatment coming before the Department are subject to the existing Department precedent, is misguided and should be rejected by the Department.

1. The Attorney General's Comments Misconstrue the Company's Request and Misapply Department Precedent.

The Attorney General's recommendation that the Company's request should be denied or delayed is predicated on the erroneous assumption that an accounting deferral that temporarily creates a regulatory asset must be limited to circumstances in which a company has incurred an extraordinary cost that would trigger a rate case in the absence of the Department's approval of the deferral.

However, it should first be noted that the Department issues accounting rulings pursuant to its general supervisory and ratemaking authority under G.L. c. 164, §§ 76 and 94. The issuance of an accounting ruling is not prescribed or constrained by statute or regulation either in relation to the process that is required to evaluate a request for an accounting ruling or the standard of review to be applied by the Department in evaluating such requests. To be sure, the majority of requests for accounting deferrals have involved the deferral of extraordinary expenses in a cost category included in base rates.³ In the case cited by the Attorney General, North Attleboro Gas Company, D.P.U. 93-229 (1994), the Department explicitly stated that it was clarifying its standard for the review

² Such a proceeding would necessarily involve discovery and evidentiary hearings as requested by the Attorney General.

³ The genesis of many requests for accounting deferrals was the Department's order in Commonwealth Electric Company, D.P.U. 88-135/151, at 21-30 (1989) in which the Department denied recovery of pre-test year extraordinary storm expenses. Thereafter, it was clear that, absent an accounting ruling, if a company incurred a large expense for a cost category included in base rates, the expense could be recovered only if the year in which the expense was incurred was a test year. The Commonwealth case did not affect the deferral and recovery of cost categories subject to reconciliation mechanisms, e.g., fuel charge, cost of gas adjustment clauses, transition costs, environmental remediation costs.

of requested deferral accounting treatment for "extraordinary pretest year expenses." D.P.U. 93-229, at 7 (emphasis added). Thus, the Department's statements in D.P.U. 93-229 do not address the circumstances where a company may be seeking an accounting treatment for something other than the recovery of an extraordinary pre-test year expense. Significantly, NSTAR's request for a deferral is not based on the existence of an extraordinary pre-test year expense, and therefore, the Attorney General's arguments (and cited precedent) do not apply.

In this case, the driving factor underlying the Company's request for an accounting treatment is the existence of an unfunded liability in the pension trust combined with the existence of a sizeable prepaid asset account balance, which has resulted from the Company's longstanding practice of making cash contributions to the fund in excess of the annual expense booked in accordance with FAS 87 and FAS 106. Specifically, the Company estimates that, by December 31, 2002, the assets in the NSTAR trust funds will be reduced to approximately \$650 million and liabilities will be equal to approximately \$825 million as a result of equity-market declines and changes in interest/discount rates, representing an unfunded liability of approximately \$175 million.

As noted in the Company's request for an accounting ruling, this shortfall creates accounting issues for the Company that will have a significant negative impact on the financial health of NSTAR and the cost of capital used to fund utility operations on behalf of the Company's gas and electric customers. Specifically, FAS 87 requires that tax-deductible pension contributions in excess of the annual expense derived under FAS 87, are to be recorded as a asset (i.e., prepaid pension expense) on the Company's books. As of December 31, 2002, NSTAR will have a prepaid pension balance of approximately \$252 million resulting from the significant tax-deductible contributions made over the past several years in excess of the expense recorded on the Company's books under FAS 87. These contributions were made in accordance with the policy directives of the Department.

Under FAS 87, this prepaid asset must be written off the Company's books as of December 31, 2002 because a portion of the Company's pension obligation is now unfunded. Since the amount of the Company's pension obligation will exceed the value of the fund assets as of December 31, 2002, the Company must also recognize an "Additional Minimum Liability" equal to the difference between the pension obligation and the value of the fund assets. The "Additional Minimum Liability" must be added to the balance of the prepaid asset account and the sum total would be recorded on the

Company's books as a charge to common equity.⁴ This charge to common equity will have the direct effect of reducing the Company's common equity on the balance sheet by \$260 million (net of taxes), which represents a 20 percent reduction in the common equity of the Company.

In this case, the Company is asking the Department to allow the Company to defer, and record as a regulatory asset the amount of its current and future Additional Minimum Liability, which represents the "unfunded" pension obligation. The Additional Minimum Liability does not represent a not a single-year expense that would be included as a test-year expense in a rate case filing. The balance of the asset account will change as the asset value of the trust fund is affected by market conditions. Accordingly, the Company's request here is not the same as those deferral cases, like North Attleboro, that were designed to address the pre-test-year extraordinary expense disallowances that were raised by the Commonwealth case.

The Attorney General cites to Fitchburg Gas and Electric Light Company, D.T.E. 02-24/-2-25 (2002) in support of the claim that "neither the booked expense amount, nor the Additional Minimum Liability are recoverable under Department precedent" (Attorney General Comments at 2), and therefore, do not qualify for deferral treatment. However, the Attorney General is confusing the issue of the requested accounting treatment with the issue of the precise mechanism of how pension and PBOP costs are recovered through rates, which will not be determined as a result of the Department's approval of the Company's requested accounting ruling.

For example, there is no question that, prudently incurred expenditures made by regulated companies for pensions and PBOPs are recoverable in rates because such costs are incurred in order to provide service to customers. Under basic cost-of service ratemaking principles, rates are set to recover a representative level of the costs that are needed to serve customers. Thus, the challenge for the Department in setting rates to recover pension and PBOP costs has been in identifying the representative level of costs to be included in rates.⁵ As noted in the Fitchburg decision, the Department has generally set rates to recover an average of annual cash contributions made by a company

⁴ In effect, these provisions of FAS 87 are designed to recognize that the Company's investment in the pension fund has been deteriorated by equity losses in the market. However, were the Department to allow the Company to defer the prepaid balance as a regulatory asset, as described below, the Company's investment would be effectively maintained until such time that additional cash contributions and market gains would mitigate the discrepancy between the value of assets held in the trust funds and the pension obligations.

⁵ This will be especially true given the current circumstances because the disparities between the FAS 87 and FAS 106 requirements for determining annual pension and PBOP expenses and the tax rules associated with the deductibility of cash contributions will be exaggerated over the next few years in light of the significant swings in the fund value that have occurred and may continue to occur as economic conditions fluctuate.

to its pension and PBOP trust funds. D.T.E. 02-24/02-25, at 110. Therefore, where a company is able to demonstrate that it makes annual contributions to its pension and PBOP funds, the Department has typically included the average of the annual contributions in rates. Boston Gas Company, D.P.U. 93-60, at 234-235 (1993). At the same time, however, the Department has expressly refrained from establishing a set policy on the calculation of pension costs for ratemaking purposes and has consistently maintained that the intricacies of the issue warrant an investigation on a case-by-case basis. Boston Gas Company, D.P.U. 96-50, at 81 (Phase I) (1996), citing, D.P.U. 95-118, at 111; D.P.U. 95-40, at 44; D.P.U. 92-78, at 46. Therefore, the Department's historical practice of including cash contributions in rates does not mean that cash contributions are recoverable and booked expenses or the Additional Minimum Liability are not. It means only that the Department has, in the past, selected cash contributions rather than booked expenses as representative of the Company's annual pension cost in setting rates.

In any event, the accounting ruling that the Company seeks here would not predetermine the characteristics of the mechanism used to determine the amount of pension and PBOP costs that would be included in rates. The accounting ruling is intended only to avoid the adverse consequences that will otherwise result from a series of unprecedented market conditions that have created a temporary accounting deficiency in its pension fund, despite the aggressive funding policies of the Company. The creation of a regulatory asset as requested, will not limit the Department's right to review (nor the Attorney General's right to challenge) the prudence or reasonableness of expenditures or the precise way in which prudently incurred pension and PBOP costs are recovered from customers.⁶ This is entirely consistent with the Department's long-held approach to the calculation of pension costs for ratemaking purposes, which allows for an investigation of the appropriate level of costs to be included in rates on a case-by-case basis in the context of a base-rate proceeding.⁷ Moreover, the Company is not seeking any change in rates through this request, and any future rate change can be accomplished only with Department approval after full review and opportunity for hearing in a rate proceeding. Therefore, despite the Attorney General's assertions, the Company's proposal comports with Department practice and precedent, and in no way contradicts the Department's

⁶ As the Attorney General points out, "the Company may elect to file a rate case as early as March of 2003 for effect after the expiration of the four year merger 'rate freeze' period" (Attorney General Comments at 2). Until that time, the rates charged to customers cannot be changed, nor will a ruling on the request for accounting treatment have the effect of making such a change. Thus, the Attorney General will have ample opportunity to address his ratemaking issues.

⁷ The Company is seeking to defer the difference between the level of pension and PBOP expenses included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106, as well as the amount of the Additional Minimum Liability, because Generally Accepted Accounting Principles ("GAAP") require the Company to book pension and PBOP obligations in a certain manner in order to qualify as a regulatory asset. However, this treatment does not dictate the structure of the ratemaking mechanism that the Department may adopt in a future proceeding to provide for the recovery of pension-related costs.

findings in the Fitchburg case, or any other rate proceeding conducted by the Department.

2. The Attorney General's "Reasons" for Denial Are Without Merit.

The Attorney General lists six reasons for the Department either to deny the request or to conduct an investigation prior to the issuance of the ruling (Attorney General Comments at 3-4). Although each of these is generally based on the mischaracterization of the request and misapplication of precedent as discussed above, in the interests of completeness and clarity, the Company will briefly address each issue separately.

- "(1) The Company has not established that the "true-up" amount is an extraordinary operating expense that Department precedent would allow as proper for deferral, Boston Gas Company, D.P.U. 89-177, pp. 7-8 (1989), or that the costs are recoverable from customers in a subsequent rate case" (Attorney General Comments at 3).*

As discussed above, the nature of the Company's request is not one in which the Company is seeking to defer extraordinary pre-test year costs, and therefore, the precedent cited by the Attorney General is not controlling in this case. However, it is well established that pension and PBOP costs are recoverable from customers in rates. Given the unique economic circumstances affecting the Company's pension fund obligations and liabilities, the Company anticipates that cash contributions, booked expenses and the prepaid asset account will exhibit an unprecedented level of variability over the next several years. The Company's request is intended to preclude the detrimental financial impacts that would be associated with a significant common equity charge and to allow an opportunity for the Department to consider the ratemaking methodology that will be used to identify the appropriate level of costs to be included in rates. Although the Department's approval of the requested accounting treatment may have the collateral effect of delaying or eliminating the filing of one or more rate cases,⁸ the Company's request is not predicated on that basis.

- "(2) The Company has not established the level of pension and PBOP expenses in the Company's rates. The relevant rates of the distribution companies were fixed by settlement or rate cases that are as much as ten years old [footnote omitted] Several of the NSTAR companies rates were set in settlements; in the settled rate cases there are no Department findings on*

⁸ As noted above, because of the Company now faces an unfunded obligation, the Company's cash contributions in 2003 and beyond will significantly exceed the expense level currently in distribution rates. Accordingly, denial of the requested accounting ruling will greatly increase the possibility that all four companies will need to seek rate relief next year.

the specific dollar amounts of individual costs, including pension and PBOPs" (Attorney General Comments at 3).

The Attorney General is correct that determining the precise level of pension and PBOP expenses that are currently in the Company's rates is complicated by rate settlements as well as industry restructuring and generation asset divestiture. However, the deferral request is based on the accounting deficiencies and expenses that must be reported under GAAP, and the amount that has been or will be included in rates is a separate ratemaking issue that will be determined by the Department in a rate proceeding. The Company is not requesting such a ruling by the Department at this juncture, nor is it necessary for the Department to make a finding with regard to this issue.

"(3) The Company has not established that the pension and PBOP expenses cannot be changed from year to year simply by making minor changes in actuarial assumptions, thus directly affecting the regulatory asset balance" (Attorney General Comments at 3).

Again, the Attorney General is raising an issue that is totally irrelevant to the request. To the extent that the actuarial assumption underlying the calculation of pension and PBOP expenses are subject to question at all, it would be only in the context of a ratemaking proceeding where the Department would be considering the appropriate level of costs to put into rates. In that regard, the Department has recognized that the calculation of pension and PBOP expenses for accounting purposes is dictated by FAS 87 and FAS 106, respectively. Western Massachusetts Electric, D.P.U. 87-260, at 44 (1988). The Department has further recognized that the adoption of FASB 87 and 106 made pension plan expense calculations less flexible. *Id.* Therefore, to the extent that the annual level of pension and PBOP expense is determined by actuarial assumptions regarding items such as future health care costs, mortality of employees and discount rates, the Company relies on independent, professional actuaries who prepare a report for the Company on an annual basis. This analysis is subject to review by the Company's outside auditors and, consistent with GAAP is based on various external indices and accounting conventions. Accordingly, the Attorney General claims in this regard should be rejected by the Department.

"(4) The Company has not established that any of the individual distribution companies will experience severe detrimental financial effects without the proposed deferral. In fact, NSTAR reported to the financial community an estimated \$200 – \$300 million impact of this accounting at end of the third quarter, yet the Company's bond rating has not changed, and the evidence does not show that the Company is having difficulty attracting capital. This transaction is not a cash outlay, rather it is an accounting accrual apparently recorded by the holding company" (Attorney General Comments at 3-4).

In its most recent Form 10-Q filed with the Securities and Exchange Commission on November 27, 2002, NSTAR made the following statements in relation to the potential equity write-off:

Assuming there is no significant change in interest rates or equity market performance for the remainder of the year, NSTAR anticipates that the after-tax charge to OCI will be approximately \$200 million to \$300 million

NSTAR anticipates filing a request with the [Department] seeking an order to mitigate the non-cash charge to OCI and the increases in expected pension and other postretirement benefit costs and cash contributions. If approved, this request could potentially allow NSTAR to record a regulatory asset in lieu of a charge to OCI.

(Form 10-Q, at 9-10).

The fact that the financial markets have not yet reacted to the Company's indications on the pension-fund situation is not surprising, nor does it represent a signal that financial repercussions will not occur once the write-off is certain. The Company is under an obligation to disclose that a write-off may take place, but ratings agencies typically do not take definitive action until the event has actually occurred, especially where the Company has indicated that a resolution is being pursued through the regulatory arena. As a result, the fact that the Company's ratings have not yet been downgraded is not indicative of the consequences that will take place if the charge to common equity occurs.

"(5) The Company has not established the actual amount of the deferral and references stale data. The Company accounted for its pension and PBOPs trust fund assets for the most recently reported quarter, September 30, 2002. Since that time the stock market has risen 18 percent. The Company has failed to indicate what the expected deferral amount will be by December 31, 2002" (Attorney General Comments at 4).

First, it should be noted that the Company's request would apply to the balance of the prepaid account as of December 31, 2002, as calculated using the most recent data available to the Company. Moreover, although the precise, final amount of the deferral cannot be known until after December 31, 2002, the change in the stock market is only one factor in the equation and, in fact, the recent rise in the stock market has had only a small impact on the overall position of the pension fund. Extremely low interest rates

Reply Letter to Mary L. Cottrell
D.T.E. 02-78
December 17, 2002
Page 10

have also increased the Company's pension liabilities and these rates remain relatively unchanged. Taking account of the asset position as of the closing of the stock market on December 13, 2002, the charge against equity on December 31, 2002 is currently projected to be \$253 million.

"(6) The Company indicated that this accounting problem is for the year 2002 and the situation will reverse in 2003. The Company, however, has not indicated what the Department should do if the situation reverses itself in 2003" (Attorney General Comments at 4).

The Attorney General has misstated the Company's position with respect to the "reversal" of the accounting entries that, absent a favorable Department ruling, will occur as of December 31, 2002. Certainly, the economic conditions over the past several years that have precipitated the accounting deficiency are unprecedented and there is every expectation that, over time, more favorable market conditions will improve the performance of the pension and PBOP trust funds. The long-term funding of pensions and PBOPs that will eventually be collected from customers will fully benefit from improved market performance, but there is nothing that will reverse the immediate harm to the Company and its customers, absent Department approval of the accounting ruling. Moreover, it is the Company's intent to establish a mechanism that ensures that customers get the benefit of any reduction in costs associated with improved market performance in the future.

- **Conclusion**

For the reasons described above, the Attorney General's objections to NSTAR's request have no basis in fact or law. The request is narrowly framed to solve the immediate and potentially devastating financial accounting problem that has resulted from the convergence of a series of market events that are totally outside of the control of NSTAR. Approval of the request results in no adverse impacts to NSTAR customers, but avoids the serious negative effect of accounting conventions. Accordingly, the Department should dismiss the Attorney General's comments and approve the requested accounting ruling.

Reply Letter to Mary L. Cottrell
D.T.E. 02-78
December 17, 2002
Page 11

Thank you for your attention to this matter.

Sincerely,

Robert J. Keegan

cc: Caroline O'Brien, Hearing Officer (seven copies)
Paul G. Afonso, General Counsel
Joseph Rogers, Assistant Attorney General
Service List

Enclosure



THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF THE ATTORNEY GENERAL

200 PORTLAND STREET
BOSTON, MASSACHUSETTS 02114

TOM REILLY
ATTORNEY GENERAL

(617) 727-2200
<http://www.ago.state.ma.us>

SENT ELECTRONICALLY, BY FAX AND MAIL

December 19, 2002

Mary Cottrell, Secretary
Department of Telecommunications and Energy
One South Station, 2nd Floor
Boston, MA 02110

RE: Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company, D.T.E. 02-78

Dear Secretary Cottrell:

On December 17, 2002, the Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company ("NSTAR" or "Company") filed a response with the Department of Telecommunications and Energy ("Department") to the comments of the Attorney General. The Attorney General continues to oppose the Company's requested accounting treatment and implicit change in Department ratemaking policy related to pensions and post-retirement benefits other than pensions ("PBOP").

NSTAR still has not demonstrated with any evidence that "detrimental financial consequences that may harm customers" will actually occur. To the contrary, recent reports from financial analysts that are attached to this letter discuss the pension and PBOP matter, yet still maintain the Company's strong credit rating. The FitchRatings Special Report on Pensions cited by NSTAR and the resulting NSTAR credit ratings indicate that this accounting adjustment will not cause detrimental financial consequences.¹ FitchRatings, while specifically recognizing

¹ The FitchRatings Special Report states on page 2:

Underfunded pension obligations, as any other real claim on cash flow, are incorporated into Fitch's debt ratings. However, it is important to note that underfunded pension positions are a long-term consideration. Pension contributions do not have an immediate

(continued...)

the Companies' pension positions, currently rates Boston Edison Company debt AA- (double "A" minus) with stable outlooks and no credit watch indications. Standard and Poors and Moody's similarly give the Companies "A" ratings with stable outlooks and no credit watch warnings. ValueLine Investment Survey still gives NSTAR stock its highest "A" rating with a stable outlook for price, and FirstCall/Thompson's Financial rates NSTAR stock a "hold." The ratings agencies clearly think that the effects of the "Alternative Minimum Liability" on the financial stability of the NSTAR utility companies will not be significant. In addition, in 2001, NSTAR booked a non-cash write-off – similar to the write-off that will be required for the pension and PBOP losses – of \$170 million for its investment in RCN, yet the Company's bond rating remained unchanged. NSTAR's claims of detrimental financial consequences that may harm customers are nothing but unsupported speculation.

Nor has NSTAR supported its claim (in footnote one) that delay to allow discovery and a hearing "is tantamount to a denial since the accounting entries must be made as of December 31, 2002." Companies frequently delay issuing financial statements for months at a time, and NSTAR could do so here.

The Company suggests that it does not seek a change in Department precedent in its November 27, 2002 request, but merely seeks a method for "the calculation of pension costs for ratemaking purposes" that departs from the "Department's historical practice of including cash contributions in rates." Company's response, p. 6. Deferrals are supposed to be approved by auditors only where there is a probability of recovery in rates. It is, therefore, misleading for NSTAR to suggest that these deferrals would have no implicit ratemaking consequences. A switch from cash to accrual accounting, coupled with a deferral and guaranteed cost recovery in a future rate case, would in fact change Department precedent and put upward pressure on rates.

The Company claims that it does not seek deferral for an "extraordinary pretest year expense" and, therefore, the case of *North Attleboro Gas Company*, D.P.U. 93-229 (1993), does not apply. Company's response, p. 3. If the Company intends to file rate cases for all four distribution companies in 2003, then there should be no reason for the deferral, since the pension and PBOP issues will be addressed by using the 2002 test year under established Department precedent. If any of the distribution companies do not file rate cases in 2003, then pension and PBOP cost recovery will be deferred until those distribution companies file rate cases. In other words, the Company then would be seeking recovery of a normal pre-test year expense, a practice long prohibited by the Department. *Nantucket Electric Company*, D.P.U. 91-106 / 91-138, pp. 20-22, 26-28 (1991). Furthermore, the Company does not address the issue raised by the Attorney General of the impact of the deferral and cost recovery request on NSTAR's four year "rate freeze." *BEC Energy / ComEnergy*, D.T.E. 99-19, pp. 5, 25, 85 (1999). The Company's proposal violates the rate freeze provisions.

¹(...continued)

effect on liquidity, but even substantially underfunded positions generally have years before the accounting gap and the funding gap converge.

Mary Cottrell
Page 3
December 19, 2002

Without citation or reference to any precedent, the Company continues to seek recovery from customers for the Company's stock market losses. The Department should deny this request.

Sincerely,

Joseph W. Rogers
Division Chief
Utilities Division

cc: Service list

Information Request AG-2-7

Please provide a copy of the legal opinion referenced on RJS, p. 3. Lines 22-23.

Response

Please see the Attachment AG-2-7.

KEEGAN, WERLIN & PABIAN, LLP

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January 2, 2003

James J. Judge
Senior Vice-President, Treasurer and
Chief Financial Officer
NSTAR
800 Boylston Street
Boston, MA 02199

Re: Accounting Ruling on Pension and Post-Retirement Benefits Other Than
Pensions, D.T.E. 02-78

Dear Mr. Judge:

On November 27, 2002, NSTAR Gas Company, Boston Edison Company, Cambridge Electric Light Company and Commonwealth Electric Company (collectively, "NSTAR" or the "Company") requested an accounting ruling from the Department of Telecommunications and Energy (the "Department") relating to NSTAR's obligations for employee pensions and post-retirement benefits other than pensions ("PBOP"). The requested accounting ruling would permit NSTAR, until otherwise ordered by the Department: (1) to defer, and to record as a regulatory asset or liability, the difference between the level of the pension and PBOP expenses that are included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106; and (2) to defer as a regulatory asset, the amount of its current and future Additional Minimum Liability to reflect NSTAR's ability to recover in rates over time its actual pension liability. The Company requested this accounting ruling pending the Department's consideration and approval of the specific recovery mechanism that will reconcile the difference between the amounts received from customers in rates and the FAS 87 and FAS 106 expenses recorded on the Company's books.

On December 20, 2002, the Department approved the requested accounting ruling. You asked our opinion as to your legal right to recover these costs as well as the probability of future recovery of the amounts that the Department has permitted to be deferred. In approving the deferral, the Department has recognized that prudently incurred pension and PBOP expenses are recoverable from ratepayers and that a mechanism needs to be developed to achieve that result. The Department's accounting ruling does not establish the specific mechanism, but recognizes that NSTAR will be proposing a detailed reconciliation method in its next rate proceeding, which we understand is scheduled to be filed during the first half of 2003. It has been our

Letter to James J. Judge

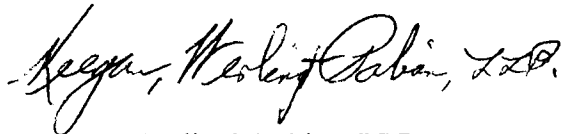
January 2, 2003

Page 2

experience that an accounting ruling that permits the deferral of costs will likely result in the subsequent reconciliation and recovery of such prudently incurred costs.

Accordingly, based on the Department's approval of the request for an accounting ruling, we are of the opinion that it is probable that the Department will approve a reconciling mechanism that will permit recovery of prudently incurred costs that are deferred in accordance with the Department's accounting ruling.

Sincerely,

A handwritten signature in cursive script, appearing to read "Keegan, Werlin & Pabian, LLP".

Keegan, Werlin & Pabian, LLP


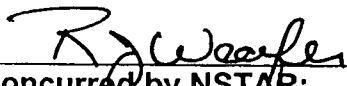
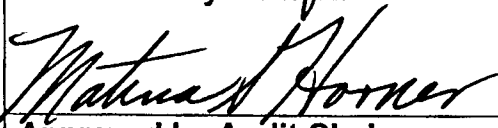
Information Request AG-2-8

Please provide a copy of the engagement letter, any letter agreements, contracts or memorandums of understanding related to the testimony submitted by Mr. Spear in this proceeding.

Response

Please see Attachment AG-2-8.

**REQUEST FOR OUT OF SCOPE AUDIT
AND NON-AUDIT SERVICES**

Type of Request (Check One):		Date Requested: June 30, 2003
<input checked="checked" type="checkbox"/> X	Out of Scope Audit Related	
<input type="checkbox"/>	Tax Services	
<input type="checkbox"/>	Other Services	
Expected Start Date: June 2003		
Expected Completion Date: December 2003		
Estimated Total Hours: 50- 125		
Estimated Total Cost: \$20 K - \$50 K (depending on DTE request)		
Description of Service Being Requested: Incremental billing in connection with professional services to be provided relating the Company's Pension & post-retirements benefits filing with the DTE. Billing rate is in accordance with the 2002 fee structure.		
		07/01/03
Requested by PWC:		Date:
		7/1/03
Concurred by NSTAR:		Date:
		7/1/03
Approved by Audit Chairperson:		Date: